



The Compliance Connection

Regulatory News for Virginia Mortgage and Consumer Finance Companies
State Corporation Commission -- Bureau of Financial Institutions

The Compliance Connection is published quarterly and is part of the Bureau's efforts to improve communication with the companies we regulate. It is distributed to Virginia mortgage, consumer finance, industrial loan and non-profit debt-counseling agency licensees, and other interested parties. It is the licensee's responsibility as a Virginia mortgage licensee to read this newsletter and to be familiar with the positions and interpretations stated herein.

Suggestions and comments concerning the newsletter or its contents should be addressed to the Bureau at P.O. Box 640, Richmond, Virginia 23218-0640 or via e-mail at: nwalker@scc.state.va.us.

Special thanks to Susan Hancock, Jane Owen, Todd Rose, Russell Spain and Dwight Stephens for their contributions to this issue!

When Are Adverse Action Notices Required?

(The following text is based on the Federal Trade Commission's (FTC) booklet "How to Write Adverse Action Notices." Although this booklet is no longer in print, an official from the FTC confirmed that the information is still accurate.)

When you deny a request for credit or close an existing credit account, this is considered adverse action. Ordinarily, you must send a written adverse action notice to the applicant or account holder. If you are unsure whether this requirement applies to your business transactions, consider the following questions.

Does This Transaction Involve Credit?

The Equal Credit Opportunity Act (ECOA) defines "credit" broadly as the right to defer payment of a debt, including the right to purchase and defer payment on property or services. The Act applies to credit extended for personal or business purposes. It applies regardless of whether credit must be repaid in installments or whether a finance charge is imposed. Thus, credit encompasses more than the mortgages, installment loans and revolving credit accounts that ordinarily come to mind.

Are You A Creditor?

After you determine that the transaction involves credit, you must decide whether you are a creditor for adverse action purposes. You are a creditor if, in the ordinary course of business, you regularly participate in the decision whether to extend credit. You participate in that decision if your actions have or may have an effect on whether an applicant receives credit (e.g., assignees or potential purchasers of the obligation).

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Points on Home Equity Lines of Credit

Did you know that when originating/brokering home equity lines of credit (HELOC), you can calculate your fees based only on the initial advance on the line versus the full amount of the line? Section 6.1-330-72 A of the Code of Virginia permits the points to be charged only on the principal amount *of the loan*. The "loan" is the amount of money advanced to the consumer. It is not the amount of the credit line that a consumer is permitted to draw upon. The full credit line amount simply represents the maximum amount of credit that is made available to the consumer. For example, if a lender extends a \$50,000 line of credit to a consumer, and the consumer draws only \$1,000, has the lender made a "loan" of \$50,000? No - the amount of the loan was only \$1,000. It is also important to point out that interest is charged on the unpaid balance of the loan, not the full credit line amount.

Please check Virginia loan files to determine if any overcharges have occurred, make any necessary refunds and modify compliance procedures accordingly.

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Annual Reports Available

The 2003 Annual Reports for Banks, Credit Unions, Savings Institutions and Trust Companies, along with the supplements for Consumer Finance Licensees, Payday Lenders and Check Cashers, are now available on the Bureau's Web site at: www.state.va.us/scc/division/banking/annual.htm. The 2003 Supplement for Mortgage Lenders and Brokers, Industrial Loan Associations, Money Order Sellers, and Nonprofit Debt Counseling Agencies will be available online soon.

Surge in Application Filings/Examinations Continue

The Bureau of Financial Institutions experienced another record year in application filings for various certificates of authority and licenses. In 2003, the total number of application filings increased to 2796 compared with 2418 in 2002 and 1325 in 2001. As you can see, application filings more than doubled over the last two years.

According to Deputy Commissioner Nick Kyros, the continuing expansion of the mortgage industry and the regulation of payday lenders are responsible for the increase in application filings. Mortgage lender and/or broker application filings (which include applications for relocations and additional offices) increased from 2030 in 2002 to 2277 in 2003. In addition, the Bureau received 276 applications from payday lenders in 2003 compared with 167 in 2002. At the end of 2003, the Bureau regulated 1899 financial institutions and licensees compared with 1556 at the end of 2002.

The Bureau's Corporate Structure and Research Section is responsible for processing applications of both depository and non-depository financial institutions including banks,

credit unions, money transmitters, consumer finance companies, nonprofit debt-counseling agencies, industrial loan associations, check cashers, payday lenders, and mortgage lenders and/or brokers. Depository institutions filed 133 applications while non-depository institutions filed 2663 applications in 2003.



The increase in application filings results in an increase in the examinations required to be conducted by the Bureau. In 2002, the Consumer Finance and Mortgage Section of the Bureau conducted 662 examinations — 83 consumer finance, 325 mortgage

broker, 106 mortgage lender, 126 mortgage lender and broker, and 22 other non-depository examinations (which include payday lenders, nonprofit debt-counseling agencies, industrial loan associations and check cashers). In contrast, 810 examinations were conducted in 2003 — 152 consumer finance, 342 mortgage broker, 94 mortgage lender, 167 mortgage lender and broker, and 55 other non-depository examinations.



Attention New Mortgage Licensees

Friday, August 20, 2004 is the date of the next orientation for new mortgage licensees. Registration packets will be sent to companies that are licensed between April 1, 2004 and June 30, 2004. Orientation begins at 9:30 a.m. at our office and concludes around 3:00 p.m. We will make every attempt to accommodate licensees who have not attended a previous session or wish to attend again; however space is limited, and newly licensed companies are given priority. Please contact Carol Foster or Jane Harris at (804) 371-9701 to inquire about seating availability.

Adverse Action Notices (continued from page 1)

Has a Consumer Made an Application for Credit?

You must provide an adverse action notice whenever you deny a credit application. This applies to **oral** as well as **written** credit applications. If you deny a telephone application, you must request the consumer's name and address in order to send the adverse action notice. If the consumer refuses to provide the necessary information, you are not required to send an adverse action notice. However, the law requires that you keep the application, along with any notations you made concerning the adverse action decision and the reasons for it, for 25 months.

Even if your company has a formal policy requiring written applications from consumers, you may, in fact, process oral applications. This happens when a consumer inquiry about credit terms turns into an oral credit application. For example, your employees may respond to a consumer inquiry by giving information about your credit terms. This exchange of information does not constitute an application. However, if your employees also evaluate the consumer's qualifications and communicate a denial to the consumer, then they have treated the inquiry as an oral application. And, as a creditor, you must comply with the adverse action notice provisions.

You want to be sure that your employees know when a consumer inquiry becomes a credit application. Credit denial raises a consumer's inquiry to the level of an oral application. Even if your employees did not obtain all the information you ordinarily require to accept an application, clearly enough information was obtained to deny it.

If you want to guard against turning an inquiry into an oral application, instruct your employees not to evaluate the qualifications of consumers who inquire about your credit terms or credit-granting criteria. Instead, your employees should encourage consumers who want to know whether they qualify for credit to submit written applications.

Inquiries that are *not* applications:

- A consumer calls to ask about loan terms and an employee explains the creditor's basic loan terms, such as interest rates, loan-to-value ratio, and debt-to-income ratio.

- A consumer asks about terms for a loan to purchase a home and tells the loan officer his income and intended down payment, but the loan officer only explains the creditor's loan-to-value ratio policy and other basic lending policies, without telling the consumer whether he qualifies for the loan.

Examples of an application:

- A consumer calls to ask about lending standards, your employee explains that you require three credit references, and, after learning that the consumer only has two references, indicates that there is no point in filling out a written application.
- A consumer stops by your office, volunteers his income, asks whether he qualifies for a loan, and an employee says his income is too low to qualify.
 - Your employees "pre-screen" consumers by refusing to take applications over the phone from those who do not meet threshold requirements such as minimum income amounts or years of employment.



Have You Taken Adverse Action?

The only remaining question is whether you have taken "adverse action" on a credit application or an existing account.

You *have* taken adverse action if:

- You refuse to grant an applicant's request for a loan or credit card.
- You make a counteroffer in which the terms or the amount differ from those the applicant requested **and** the applicant rejects the counteroffer. If you were to require a cosigner or a shorter repayment period than requested, for example, you would be making a counteroffer.
- You tell consumers who ask about obtaining credit that they do not meet your underwriting criteria.

You have *not* taken adverse action on a request for credit or on an existing account if:

- You make a counteroffer and the applicant accepts the offer.
- You close an account or change its terms because of inactivity, current delinquency, or default on the account.

“Dual Fees” Still Prohibited

Recently, the Bureau has received information that some mortgage companies are contacting real estate brokers and agents and telling them that several states now allow real estate agents to receive a fee for taking an application and providing initial loan documents in addition to receiving a real estate commission. Please note that Section 6.1-422C of the Code of Virginia prohibits “dual compensation” with limited exceptions (see explanation below). Real estate agents who engage in mortgage broker and/or lender activities (please refer to the definitions of “mortgage lender” and “mortgage broker” in §6.1-409 of the Code of Virginia) must be licensed by the Commission, be a bona fide employee of a licensed mortgage company, or be exempt from licensing under §6.1-411 of the Code of Virginia. It should also be noted that Section 3500.14 of Regulation X (RESPA) also prohibits kickbacks and unearned fees.



Section 6.1-422C prohibits a mortgage broker from receiving compensation for negotiating, placing or finding a mortgage loan where the mortgage broker, or any person affiliated with the mortgage broker has also acted as a real estate broker, agent or salesman in connection with the sale of real estate which secures the loan, **unless** the mortgage broker was licensed by the Commission prior to February 25, 1989. If the mortgage broker was licensed prior to this date, the prohibition is inapplicable as long as the proper disclosure is given in writing at the time the mortgage broker services are first offered to the borrower (see “Notice” under §6.1-422 B (5)).

An “affiliated person of a mortgage broker” means any person which is a subsidiary, stockholder, partner, trustee, director, officer or employee of a mortgage broker and any corporation ten percent or more of the capital stock of which is owned by a mortgage broker or by any person which is a subsidiary, stockholder, partner, trustee, director, officer or employee of a mortgage broker.

CSBS Elects Officers for 2004-2005

Mississippi Commissioner of Banking and Consumer Finance **John S. Allison** took office as Chairman of the Conference of State Bank Supervisors (CSBS) at the organization’s 103rd Annual Meeting and Conference in Rancho Mirage, CA., today. Allison succeeds Oklahoma Bank Commissioner **Mick Thompson**, who continues on the CSBS Board as Immediate Past Chairman.

CSBS members also elected **D. Eric McClure**, Missouri Commissioner of Finance, as Chairman-elect. McClure will take office as CSBS Chairman at the 104th Annual Meeting in June 2005. Virginia Commissioner of Financial Institutions **E. Joseph Face** was elected Vice Chairman. Wyoming State Banking Commissioner **Jeffrey Vogel** was elected Secretary, and North Dakota Commissioner of

Financial Institutions **Timothy J. Karsky** enters his second year of a two-year term as CSBS Treasurer.

“State bank supervisors play a vital role in ensuring that our nation will continue to benefit from our dual banking system,” said Allison. “The Conference of State Bank Supervisors is the only national organization dedicated to advancing the state bank charter.”

“Over 73 percent of the nation’s banks are state-chartered,” Allison added. “That fact points out that the dual banking system is alive and well and undergirds the organization’s mission: to champion a system that offers competitive chartering options, efficient and effective supervision, and a lower cost of regulation for all banks.”

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Press Release Issued: Provides Guidance to Consumers about Lock-ins

A press release entitled “Mortgage Rate Lock-ins Not Always such a ‘Lock’” was issued on May 11, 2004 and can be found on the Bureau’s Web site at www.state.va.us/scc/division/banking. The release provides tips for consumers for understanding the lock-in process and the potential pitfalls that can occur in a rising interest rate market.

License Update

The following is a list of companies that have surrendered their licenses, had their licenses revoked, had an application denied, or been fined by the Commission since February 15, 2004. This list should be helpful to keep track of companies with which you do business. These lists are accurate as of May 15, 2004. Call the Bureau if you have a question concerning a recent denial, surrender or regulatory action taken by the Commission. A list of current mortgage licensees is available on our Web site at <http://www.state.va.us/scc/division/banking/vamortgagelist.htm>

Mortgage License Surrenders

MLB – 76 Liberty Financial Services, Inc., surrendered its lender authority 2/16/04 - NOW LICENSED AS MB - 2489

MB – 171 Jeffrey Dale Chandler - 2/23/04

MB – 2114 Bycos LLC - 2/25/04

MB – 1797 Wholesale Express Mortgage Corporation, Inc. - 2/26/04

MLB – 435 The Merion Group, L.C., surrendered its lender authority 2/26/04 - NOW LICENSED AS MB - 2495

MB – 2200 MJD Diversified Financial Services, Inc. d/b/a Integrity First Mortgage - 3/2/04

MLB – 904 Fidelity & Trust Mortgage, Inc. - 3/2/04

MB – 1412 DH Capital, LLC - 3/5/04

MLB – 300 K. Hovnanian Mortgage, Inc. - 3/12/04

MB – 957 CitiStreet Mortgage Services, Inc. - 3/16/04

MB – 754 First Mid Atlantic Mortgage Corporation, Incorporated - 3/18/04

MB – 1508 Nancy G. Philpott d/b/a Piedmont Mortgage Services - 3/23/04

MB – 2283 Lakeside Mortgage, LLC - 3/31/04

MB – 1602 First Virginia Carolina Mortgage, Inc. - 3/31/04

MLB – 682 Advantage Investors Mortgage Corporation - 3/31/04

ML – 471 Washington Mutual Finance of Virginia, LLC - 4/1/04

MLB – 403 Chesapeake Investment & Mortgage Corporation - 4/6/04

MB – 1939 First Source Financial USA, Inc. (used in VA by First Source Financial USA) - 4/8/04

ML – 236 Woodland Capital Corp. - 4/13/04

MLB – 755 Oakwood Acceptance, LLC (used in VA by Oakwood Acceptance Corporation, LLC) - 4/13/04

MLB – 487 Independent Realty Capital Corporation - 4/13/04

MB – 1429 Monument Funding Group, Inc. - 4/19/04

MB – 1873 Mortgagebot LLC - 4/23/04

MB – 751 Pumphrey Financial Group, Inc. d/b/a American Mortgage Services, A Division of Pumphrey - 4/27/04

MB – 1263 Old Stone Mortgage Corporation - 4/30/04

MB – 1829 Victoria Jean Johnson d/b/a Luxury Loans - 4/30/04

Mortgage Licenses Denied

MB – 2335 Independent Mortgage Corp. – 4/20/04

Mortgage Licenses Revoked

MB – 1284 Loan Consolidation and Refinancing Company, LLC – revoked 5/5/04 for failure to continuously maintain the surety bond pursuant to §6.1-413 of the Code of Virginia

MB – 917 Ransford K. Fumey & Abdulai Conteh t/a Landmark Financial & Accounting Associates – revoked 5/12/04 for failure to continuously maintain the surety bond pursuant to §6.1-413 of the Code of Virginia and for various other violations of the Mortgage Lender and Broker Act

Mortgage Penalties Paid

Stacy Snyder – paid \$1,000 on 3/15/04 for failure to obtain Commission approval prior to acquiring 40% of the stock of CapitalBanc Mortgage Corporation (MLB – 708), in violation of §6.1-416.1 of the Code of Virginia

MLB – 822 Challenge Financial Investors Corp. d/b/a Challenge Mortgage – on 4/13/04 paid \$25,000 settlement for various violations of the laws and regulations applicable to the conduct of its licensed business

CSBS Elects Officers (continued from page 4)

"This is an incredibly important year for CSBS and for all state banking regulators to work together on issues vital to our nation's financial services industry."

Supervisors representing the districts will be:

- District I - Delaware State Bank Commissioner **Robert Glen**
- District II - Indiana Director of Financial Institutions **Charles W. Phillips**
- District III - Louisiana Deputy Commissioner of Financial Institutions **Doris Gunn**
- District IV - Kansas Commissioner of Banking **Clancy Norris**
- District V - Utah Commissioner of Financial Institutions **Ed Leary**

Chairman Allison appointed Arkansas State Banking Commissioner **Robert H. (Bunny) Adcock** and California Commissioner of Financial Institutions **Howard Gould** to at-large positions on the Board.

Judi Stork, Kansas Deputy Commissioner of Banking, who heads the Education Foundation of State Bank Supervisors, continues as a member of the Board. Other members of the Board of Directors are Bankers Advisory Board co-Chairmen, **Gary Nelson**, Chairman and CEO of First Texas Bancorp., Inc, Georgetown Texas and **Thomas B. Gronstal**, Iowa Superintendent of Banking; International Bankers Advisory Board co-Chairmen **Fernando Capablanca**, President, Banco Credito Inversiones, Miami, Florida; **Diana L. Taylor**, New York State Superintendent of Banks; North Carolina Commissioner of Banks **Joseph A. Smith Jr.**, Chairman of the CSBS Legislative Committee; Tennessee Commissioner of Financial Institutions **Kevin Lavender**, Chairman of the CSBS Regulatory Committee; and **David Sorrell**, Commissioner for the Georgia Department of Banking and Finance, who chairs the CSBS Technology Committee.



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IMPORTANT REGULATORY INFORMATION ENCLOSED!